

**STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE
300 Capitol Mall, Suite 1700
Sacramento, California 95814**

**File No. RH03032089
May 18, 2004**

SUBJECT: AUTOMOBILE INSURANCE FRAUD PROGRAM

INITIAL STATEMENT OF REASONS

The Insurance Commissioner of the State of California (Commissioner) proposes to amend section 2698.61 and 2698.62 of Article 4, Subchapter 9, of Chapter 5 Title 10 of the California Code of Regulations (CCR) regarding the assessment for the funding of organized automobile insurance fraud. The purpose of the proposed adoption is to implement, interpret and make specific the provisions of the California Insurance Code (CIC) section 1872.8 requiring the Commissioner to assess and distribute to California district attorney's certain funds assessed from automobile insurers to fund investigation and prosecution of automobile insurance fraud.

DESCRIPTION OF THE PUBLIC PROBLEM

The Commissioner proposes to amend title 10 CCR sections 2698.61 and 2698.62 regarding the program for investigation and prosecution automobile fraud. The purpose of the proposed amendment is to implement, interpret and make specific the provisions of the California Insurance Code (CIC) section 1872.8 which requires the Commissioner to assess insurers up to \$1.00 for each vehicle it insures under a policy of insurance in this state and distribute those funds to California district attorneys and the CDI for the purpose of prosecuting automobile insurance fraud cases.

AB 1050, Chapter 885, Statutes of 1999, was signed by the Governor on October 9, 1999 creating the Organized Crime Prevention and Victim Protection Act of 1999. AB 1050, inter alia, added CIC 1874.8 1874.81 as well modifying existing CIC section 1872.8. In adopting AB 1050, the Legislature made the following findings and declaration of purpose:

Section 1. (a) This act shall be known as the Organized Crime Prevention and Victim Prevention Act of 1999.

“(b) The Legislature finds that organized automobile fraud activity operating in the major urban centers of the state represents a significant portion of all individual fraud-related automobile insurance cases. These cases result in artificially higher insurance premiums for core urban areas and low-income areas of the state than for other areas of the state. Only a focused, coordinated effort by all appropriate agencies and organizations can effectively deal with this problem.”

CIC section 12921 requires the Commissioner to enforce the provisions of the Insurance Code and other laws regulating the business of insurance in the State of California. CIC section 1872.8, requires the Commissioner to establish an annual assessment on each automobile for which a policy of insurance has been issued in order to fund the activity of the Commissioner, the California Highway Patrol and county District Attorney's Offices.

The proposed amendments are necessary to implement, interpret and make specific the provisions of CIC sections 1872.8 and title 10, CCR sections 2698.61 and 2698.62. The proposed action would amend the existing section by deleting the provisions in subsection (a) providing for the prorating of the payment in incremental payments and by adding text expressly proscribing the prorating of the assessment or the payment of the assessment. The proposed action would make a conforming amendment subsection (b) by deleting provisions permitting the calculation of the assessment on a prorated basis and adding language providing for the payment of the full assessment for vehicle on which a policy of insurance was issued during each quarter of the calendar year r any part thereof. The proposed amendment would further provide a method for tracking verification of the vehicle/policy count.

STATEMENT OF SPECIFIC PURPOSE

The specific purpose of each adoption, and the rationale for the determination that each adoption is reasonably necessary to carry out the purpose for which it is proposed, together with a description of the public problem, administrative requirement, or other condition or circumstance that each adoption is intended to address, is as follows:

Section 2698.61

Adds a definition for the terms "in force" and "vehicle identification number" ((k) and (r), respectively) and makes appropriate adjustment to the existing definitions for the insertion of the added provisions.

Rational for Necessity

The term "in force" as defined under 2698.61, subsection (k) is necessary to make clear that an assessment is due under this program when the issuance of a policy of insurance is represented by a covering note or binder. The proposed amendment to section 2698.661, subsection (r) of is necessary to provide uniform and specific definition of the term vehicle identification number by their vehicle specific "vehicle identification number."

Section 2698.62

Deletes provisions of subsection (a) providing that the amount, calculation and remittance of the assessment may be undertaken on an annualized and prorated basis. Adds a specific provision that an assessment may not be prorated either in amount assessed or remitted.

Deletes provisions of subsection (b) providing a method for the calculation of the assessment on a prorated basis. Adds text to subsection (b) that provides a method for the calculation and remittance of the assessment on a quarterly but non-prorated basis. Further adds to the existing provision that insurer's will certify that they have calculated the assessment in conformity with the provisions of this section.

Renumbers existing subsection (c) to subsection (d). Adds subsection (c) requiring insurers to maintain, in an indefinable data file, information necessary for the verification of assessment calculation, which includes the specific vehicle identification number, policy number and dates of coverage.

Renumbers existing subsections (d) to subsection (e). Adds to renumbered subsection (d) subpart (4) providing an exclusion from assessment vehicles for which a policy has been written but never put in force (i.e., a "flat cancellation").

Renumbers existing subsection (e) to subsection (f).

Rational for Necessity

CIC section 1872.8 does not specify methodology for the calculation and payment of this assessment. The existing regulations permit prorating in the calculation and remittance of the assessment and also do not expressly require insurers use a specific and uniform method of counting vehicles or documenting their count in a manner that will permit efficient payment and verification.

After more than two years implementing the existing regulations, the Commissioner has determined that the existing regulations have resulted in inconsistent and inaccurate methods of calculating the assessment and may have also resulted in a significant reduction of the gross amount of the assessment.

The proposed amendments, provide a specific, clear and uniform method for undertaking the calculating of the assessment, by requiring each insurer to calculate and pay the assessment on a vehicle/policy specific non-prorated basis, will result in a program that is both accurate and verifiable method and at a fair and appropriate level. However, because using non-prating method to collect an annual assessment based on a calendar or budget year would result in insurers being required to remit a full assessment on the same vehicle and same policy within a 12-month period. While not specifically proscribed by the provisions of CIC 1872.8, in order to mitigate what may appear to be an unfair and harsh result and to provide a specific and clear interpretation of the term, these amendments will apply an interpretation of the term "annual" for the purpose of calculating the assessment, to be a 12-month (four quarter) period including the quarter the assessment was due rather than a calendar or budget year.

The extant regulation require insurers to provide verification of vehicle count used determine the amount of assessment due. However, the provisions of the existing regulations do not require a specific and uniform method for such identification. The

proposed regulation will clarify and make more specific the provisions CIC 1872.8 by specifying that vehicle shall be identified on a policy/vehicle specific basis and that such information is retained in a discrete file.

Under the existing regulations, insurers are required to certify under penalty of perjury that the vehicle count is accurate. This requirement promotes accuracy and responsibility by ensuring the awareness of the requirement and responses by an officer of the insurer. The proposed amendments will require a uniform methodology for calculating the assessment. Accordingly, this amendment will extend the certification to cover the methodology employed is appropriate to ensure the awareness, accuracy and responsibility of the company for the need to conform to the prescribed method.

Finally, some insurers have questioned and/or indicated a need to clarify whether an assessment was due for vehicles insured under a policy that had been written but had never gone into effect (otherwise known as a “flat cancel”.) The Commissioner does not interpret the assessment statute as requiring the remittance of an assessment where the policy may have been but never put in force. Accordingly, in order to provide clarity on this point, an express exclusion is appropriate.

IDENTIFICATION OF STUDIES

The Commissioner has not relied on any technical, theoretical, or empirical study or report, or similar document, proposing the adoption of these regulations. The CDI has prepared and reviewed an economic study of the possible impact of allowing the assessment to be calculated and remitted on a pro rata basis. That study is entitled “Predicting the Department Revenue from Fraud Auto Assessment: An Economic Model Approach”. A redacted version (removing the names of the specific insurers and other confidential information) will be included in the rule making file.

SPECIFIC TECHNOLOGIES OR EQUIPMENT

Adoption of this regulation as proposed would not mandate the use of specific technologies or equipment.

ALTERNATIVES

In accordance with Government Code Section 11346.5(a)(12) the CDI must determine that no alternative considered by the CDI would be more effective in carrying out the purpose for which the action was taken or would be as effective and less burdensome to affect private persons than the emergency action. These regulations are to implement, interpret and make specific a statutorily prescribed program. The Commissioner has not identified any effective alternative, or any equally effective or less burdensome alternative to the regulation, at this time. The public is invited to submit such alternatives during the public comment process.

EVIDENCE RELIED UPON TO SUPPORT INITIAL DETERMINATION THAT REGULATION WILL NOT HAVE A SIGNIFICANT ADVERSE ECONOMIC IMPACT ON BUSINESS (GC 11346.2(B)(4))

This requirement does not effect the amount of the assessment due as required by the by existing statute. This regulation would only establish a more specific methodology for the calculation and collection and verification of the existing assessment.